AMSEC Raising the bar

Asian Markets Securities Pvt. Ltd.

Allahabad Bank

Sector: Banking

Buy

CMP : Rs. 234
Target Price: Rs. 293

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Nifty: 6,143; Sensex: 20,445

Key Stock Data	
BSE Code	532480
NSE Code	ALBK
Bloomberg	ALBK IN
Shares O/s Mn	446.7
Market cap (Rs. Bn)	104.5
52-week High/Low	237/104
3-m daily average vol.	13,39,987

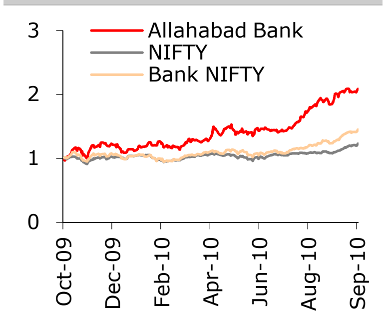
Price Performance

(%)	1m	6m	12m
Allahabad	9.7	63.0	104.8
CNXBANK	15.4	32.1	41.7
NIFTY	12.3	16.1	20.9

Shareholding Pattern

(%)	Jun10	Mar10	Dec09
FII	14.0	13.1	13.3
Institutions	14.1	15.6	15.1
Promoters	55.2	55.2	55.2
Others	11.7	12.1	12.9
Totals	100.0	100.0	100.0

Price Performance Rel. to Benchmarks



Summary

Expected to outperform peers

Allahabad Bank is on a strong growth trajectory and is expected to outperform the Indian banking industry. Its strong distribution network and vast customer base in CASA-rich states enable it to leverage significant business opportunities in the current rising interest rate scenario. This along with a balanced loan portfolio and high proportion of low-cost funds (34% of total deposits) should help the bank earn better margins compared with other public sector banks. In addition, Allahabad Bank is well positioned with good asset quality backed by provisioning of more than 70%.

The stock trades at FY11E and FY12E BV of 1.31x and 1.09x and P/E of 6.96x and 5.36x respectively. We value the stock at 1.5x FY12E BV to arrive at target price of Rs293, which implies 25% potential upside from the current level. We initiate coverage with a **'Buy'** recommendation.

Investment Highlights

- **Strong and efficient liabilities franchise will be key driver**
  We foresee minimum impact on Allahabad Bank's margins in the current interest rate scenario as it has well-diversified liabilities franchise and is in a position to fund future loan growth with optimum mix of low-cost deposits and term deposits.
- **Expected to maintain best-in-class cost to income ratio**
  The bank's cost to income ratio has improved to 38.83%; we expect further improvement as it has relatively lower liabilities arising from implementation of second pension plan and incremental benefits from implementation of CBS.
- **Business is expected to grow at a robust pace**
  Allahabad Bank's loans and deposits are expected to grow at 24% and 18.5% in FY11, which is higher than expected industry growth. The bank's CASA ratio is estimated to improve to 35% in FY11 from 34%in FY10.
- **Best-in-class asset quality**
  Allahabad Bank's asset quality is comfortable with gross and net NPAs at 1.5% and 0.41% respectively as of June 2010. The restructured assets portfolio is also demonstrating remarkable performance; it came down to 4.3% of advances in June 2010 compared with 6.9% in June 2009.
- **Valuations will improve on better operational performance**
  We estimate earnings to grow at 27% CAGR over FY10-12E, led by improvement in NII and healthy fee income growth. We believe the market has not fully recognized the bank's fundamental strengths and it deserves a better rating. We recommend **"BUY"** with a one-year target price of Rs293.

Financial Snapshot

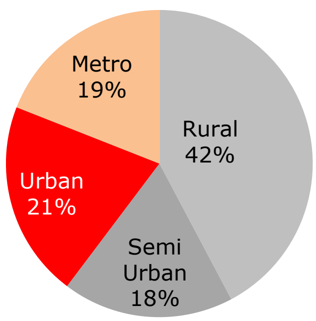
Rs bn	NII	Other Income	Ope Profit	Net Profit	Deposit	Credit	Total Assets	NIM (%)	Avg. ROA (%)	Avg. ROE (%)	EPS (Rs)	BV (Rs)	P/E (x)	P/B (x)
FY09	21.6	11.4	19.0	7.7	850	588	976	2.40	0.85	13.88	17.2	131.0	2.26	1.79
FY10	26.5	15.2	25.5	12.1	1,061	716	1,217	2.37	1.10	19.15	27.0	151.2	5.29	1.55
FY11E	34.2	16.5	32.0	15.0	1,257	888	1,445	2.55	1.24	21.71	33.6	178.3	6.97	1.31
FY12E	42.0	19.1	39.7	19.5	1,508	1,074	1,738	2.60	1.22	22.18	43.6	214.9	5.37	1.09

Investment Rationale

Saving deposits constitute 77% of total CASA deposits, which are a relatively more reliable source of low-cost funding

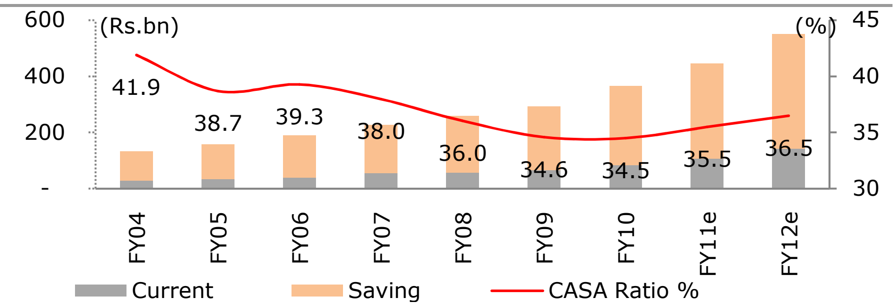
- **Strong and efficient liabilities franchise will be key driver**
  With a strong distribution network, Allahabad Bank is expected to deliver improved operating performance in coming quarters. Cost of deposits is expected to increase at a lower pace compared with peers due to higher proportion of low cost deposits and well-placed liabilities franchises.

Fig 1: Branch Distribution



Source: Company

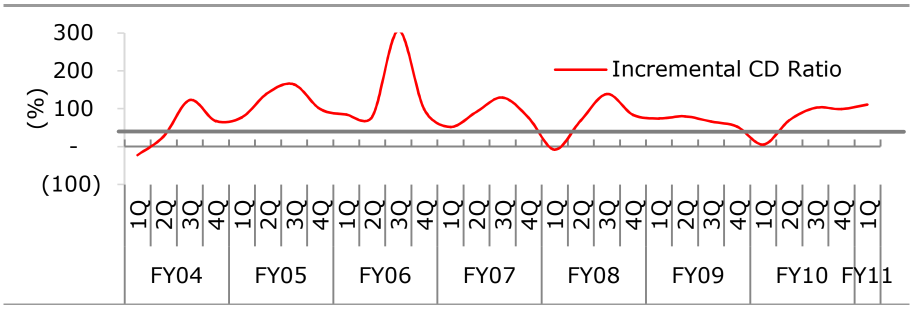
Fig. 2: Saving deposits contribute 77% to low-cost deposits



Source: Company, AMSEC

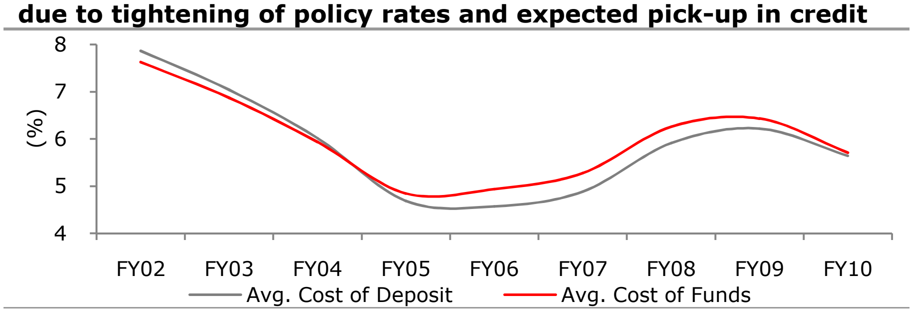
Normally, banks face increased pressure on cost of deposits in a rising interest rate scenario, which becomes intensified if the banking system is seeing high credit disbursement. A similar situation was faced by many banks in India in FY06-08, when they experienced a decline in their net interest margins, led by sharp increase in cost of funds.

Fig. 3: Incremental CD ratio of above 70% negatively impact cost of funds of banks



Source: Company, AMSEC

Fig. 4: Cost of funds of banking system is expected to move up due to tightening of policy rates and expected pick-up in credit



Source: Company, AMSEC

The current incremental credit deposit ratio of the banking system is hovering above 70%, which indicates relatively strong demand in credit disbursement compared with deposit mobilization. We see this trend continuing in FY11 and FY12 as economic activity is expected to pick up substantially in coming years.

The bank plans to open at least 100 branches each year over the next 2-3 years

Table 1: Cost to Income Ratio (1QFY11)

Bank Name	CI Ratio (%)
Indian Bank	34.7
Oriental Bank	35.4
Corporation Bank	35.6
Allahabad Bank	**38.7**
Canara Bank	39.7
UCO Bank	42.7
United Bank	45.9
Andhra Bank	46.0
Vijaya Bank	49.0
Dena Bank	49.0
Syndicate Bank	50.2
Central Bank	51.1
B OM	52.1
IOB	66.0

However, we foresee minimum impact on Allahabad Bank's margins in the current scenario as it has well diversified liabilities franchises and is in a position to fund future loan growth with an optimum mix of low-cost deposits and term deposits. This gives the bank an edge over other public sector and private sector peers.

- **Expected to maintain best-in-class cost to income ratio**
  Allahabad Bank has been able to reduce its cost to income ratio significantly despite the ongoing CBS implementation and its aggressive branch network expansion plan. The bank's cost to income ratio improved to 38.83% in FY10 from 53.4% in FY05. We expect the ratio to improve further as the bank has relatively lower liabilities arising from implementation of second pension plan and additional benefits from implementation of CBS.

  The bank is targeting 100% CBS implementation by December 2010. However, the aggressive branch network expansion plan would have a negative impact on the cost to income ratio.

- **Asset-liability gap indicates steady improvement in margins**
  An analysis of the bank's assets-liability position suggests that NIMs will steadily improve over the next few quarters. The maturity pattern of the bank's deposits as of 31 Mar,10 indicates that 48.9% of its deposits are pegged for the long term (more than one year). This gives the bank a major advantage in the rising interest rate scenario. Further, it has excess liquidity of ~Rs70bn, which is currently deployed in low-yielding short-term securities. Re-deployment of these funds will result in further improvement in margins.

Table 2: Maturity pattern of assets and liabilities

Maturity pattern	Deposits				Advance				Investment			
	FY2009-10				FY2009-10				FY2009-10			
	Outstanding as on		Average Maturity		Outstanding as		Average Maturity		Outstanding as on		Average Maturity	
	Amount (Rs mn)	% of Total	Days	Weighted Avg.	Amount (Rs mn)	% of Total	Days	Weighted Avg	Amount (Rs mn)	% of Total	Days	Weighted Avg
1 Day	10,663	1.0%	1	0.0	15,735	2.2%	1	0.0	200	0.1%	1	0.0
2-7 Days	35,316	3.3%	5	0.1	5,000	0.7%	5	0.0	99	0.0%	5	0.0
8 - 14D	33,854	3.2%	11	0.4	6,754	0.9%	11	0.1	399	0.1%	11	0.0
15 - 28D	32,307	3.0%	22	0.7	21,122	2.9%	22	0.6	5,406	1.4%	22	0.3
29 D - 3M	176,815	16.7%	60	9.9	60,526	8.5%	60	5.0	39,084	10.2%	60	6.1
>3 M - 6M	111,126	10.5%	136	14.2	74,057	10.3%	136	14.0	3,318	0.9%	136	1.2
>6 M - 1Y	141,918	13.4%	273	36.5	47,748	6.7%	273	18.2	3,063	0.8%	273	2.2
>1 Y - 3Y	**452,687**	**42.7%**	**730**	**311.6**	**230,781**	**32.2%**	**730**	**235.3**	21,003	5.5%	730	39.9
>3 Y - 5Y	39,406	3.7%	1,460	54.2	70,697	9.9%	1,460	144.1	33,857	8.8%	1,460	128.6
>5 Yrs	26,464	2.5%	1,825	45.5	**183,630**	**25.6%**	**1,825**	**468.0**	**277,857**	**72.3%**	**1,825**	**1,319.6**
Total	**1,060,558**	**100%**		**473.2**	**716,049**	**100%**		**885.5**	**384,286**	**100%**		**1,497.8**
Weighted Average Maturity in Years				**1.30**				**2.43**				**4.10**

Source: Company, AMSEC

Fig. 5: NIM 1QFY11 (%)

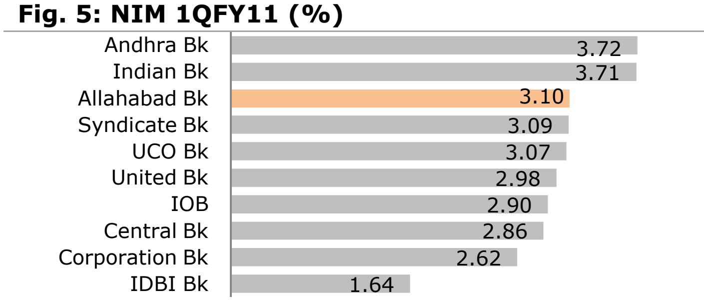
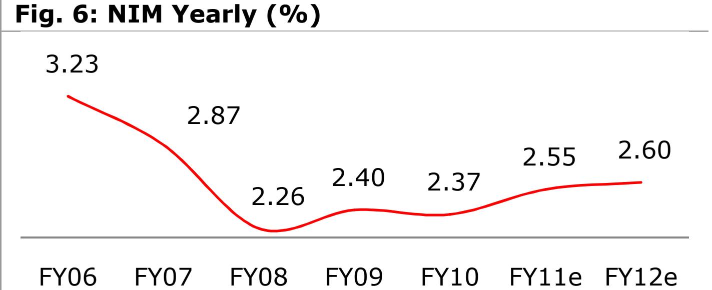


Fig. 6: NIM Yearly (%)



Source: Company, AMSEC

Business is expected to grow at a robust pace

Gross bank credit of the banking industry is expected to grow ~20% in FY11, led by healthy demand from domestic corporate, SME and retail segments. Allahabad Bank's credit and deposits grew 24.1% YoY and 22.2% YoY in 1Q FY11 versus an average 21.7% YoY and 14.9% YoY respectively for the overall banking industry. Management intends to maintain this momentum and is taking strategic initiatives to ensure rapid growth. Further, the bank's lucrative branch profile gives it significant business opportunities by allowing it to leverage its wide network in eastern and northern India to raise low-cost deposits and lend to high-yielding credit businesses.

Fig. 7: Trend in deposit mobilization

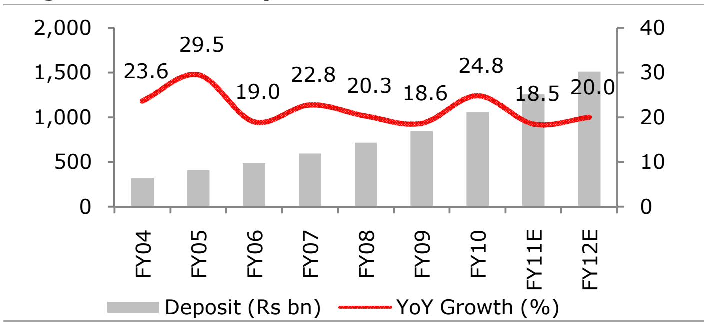
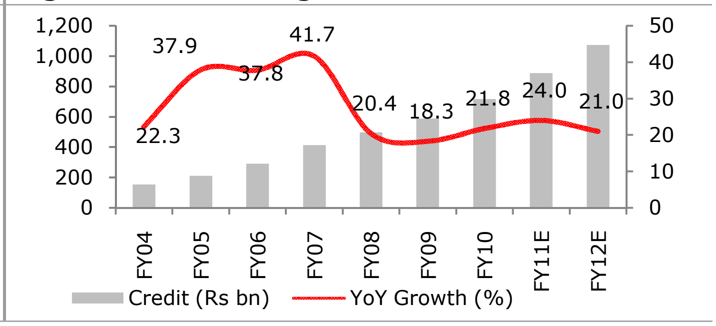


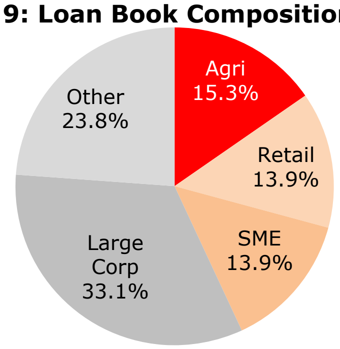
Fig. 8: Trend in loan growth



Source: Company, AMSEC

We expect Allahabad Bank's loan book and deposits to grow at 24% and 18.5% in FY11, above industry growth. The bank's CASA ratio is expected to improve to 35% in FY11 compared to 34% in FY10. Planned branch expansion, a strong CASA base and better pricing power should ensure stable margins for the bank.

Fig 9: Loan Book Composition



Source: Company

Diversified loan portfolio to further tilt toward large corporate and SME segments

Allahabad Bank has a well-diversified loan portfolio spread across the corporate, retail and agriculture segments. The loan portfolio is expected to further tilt toward mid-corporate, SME and retail loans. Allahabad Bank's loan book grew at 27.6% CAGR in FY05-10 and it is expected to grow at 22.5% CAGR during FY10-12. As of end-June 2010, the loan book stood at Rs757.2bn, marking credit growth of 24.1% YoY.

Table 3: Allahabad Bank loan portfolio

Sector	As on (Rs mn)				YoY Growth (%)			Incremental Contribution (%)		
	Mar-08	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Apr-Jun 10
Agri	84,170	95,680	115,670	115,980	13.7	20.9	21.1	12.6	15.4	0.9
Retail	73,940	84,010	100,820	105,180	13.6	20.0	26.0	11.0	12.9	13.3
SME	46,100	55,080	97,710	104,980	19.5	77.4	75.9	9.8	32.8	22.2
Large Corp	132,970	194,400	239,240	250,700	46.2	23.1	20.6	67.3	34.5	34.9
Other	165,940	165,260	170,930	180,340	-0.4	3.4	10.4	-0.7	4.4	28.7
Total	**503,120**	**594,430**	**724,370**	**757,180**	**18.1**	**21.9**	**24.1**	**100.0**	**100.0**	**100.0**

Source: Company, AMSEC

The bank is aggressively pursuing loan book expansion in SME and large corporate segments.

The SME loan book grew 77.4% in FY10 and contributed 32.8% to incremental loans. Aggressive loan growth in this segment is positively impacting yield on funds of the bank. We expect strong growth in the SME loan portfolio in FY11 and FY12 as the bank is aggressively pursuing this segment and has taken various strategic initiatives in this regard. The large corporate segment grew 23.1% YoY in FY10 and contributed 34.5% to net incremental loan. The power sector contributed a major proportion of incremental disbursement in the large corporate segment and accounted for 11.2% of the total advances portfolio of the bank as of

June 30 2010. Going forward, we expect this trend to continue as major chunk of sanctions pending disbursement are to the power sector.

Table 4: Industry-wise growth of Allahabad Bank's loan book

Sector	As on (Rs mn)				YoY Growth (%)			Incremental Contribution (%)		
	Mar-08	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Apr-Jun 10
Power	3,382	5,129	7,433	8,467	51.7	44.9	47.0	38.6	40.0	56.4
Basic Metal	2,744	3,215	4,638	5,546	17.2	44.3	36.4	10.4	24.7	49.5
Engineering	1,285	2,124	3,166	2,957	65.3	49.1	40.5	18.5	18.1	-11.4
Chemical	1,365	1,484	2,172	2,184	8.7	46.4	36.5	2.6	11.9	0.7
Textiles	1,428	1,768	1,853	1,837	23.8	4.8	-5.3	7.5	1.5	-0.9
Tele-comm	967	1,849	1,651	1,740	91.2	-10.7	16.5	19.5	-3.4	4.9
Food Pro.	606	721	1,132	1,143	19.0	57.0	41.6	2.5	7.1	0.6
Minning	43	57	67	71	32.6	17.5	34.0	0.3	0.2	0.2
Total	**11,820**	**16,347**	**22,112**	**23,945**	**38.3**	**35.3**	**33.0**	**100.0**	**100.0**	**100.0**

Source: Company, AMSEC

Under retail loans, the bank is predominately focusing on housing loans, trade and education loan segments, which are high-yielding assets with relatively lower risk profile. The bank's exposure in unsecured personal loans is very low as it contributes only 2.3% to the total advances portfolio as of June 30 2010.

Table 5: Retail loan growth of Allahabad Bank's loan book

Sector	As on (Rs mn)				YoY Growth (%)			Incremental Contribution (%)		
	Mar-08	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Jun-10	Mar-09	Mar-10	Apr-Jun 10
Housing	42,250	47,280	60,160	62,660	11.9	27.2	27.4	50.0	76.6	57.3
Personal	17,240	18,930	17,860	17,980	9.8	-5.7	6.4	16.8	-6.4	2.8
Education	4,630	6,410	8,260	8,610	38.4	28.9	27.6	17.7	11.0	8.0
Trade	5,050	5,640	6,380	7,180	11.7	13.1	51.5	5.9	4.4	18.3
Other Retail	4,770	5,750	8,160	8,750	20.5	41.9	48.1	9.7	14.3	13.5
Total	**73,940**	**84,010**	**100,820**	**105,180**	**13.6**	**20.0**	26.0	**100.0**	**100.0**	**100.0**

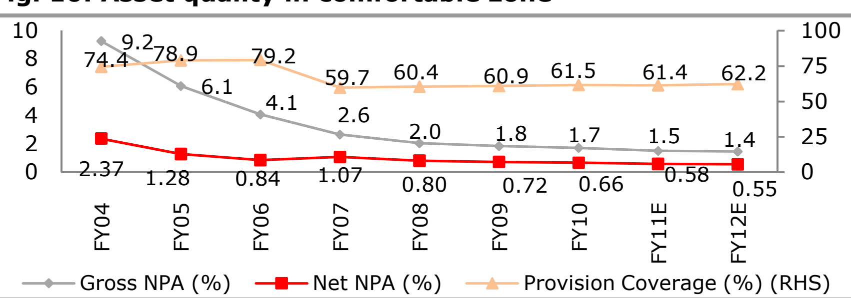
Source: Company, AMSEC

- **Best-in-class asset quality**

Slippage ratio came down substantially to 1.71% in FY10, compared with 2.46% in FY04.

Allahabad Bank's asset quality is comfortable with gross and net NPA ratios of 1.5% and 0.41% respectively as of June 2010. Aggressive write-offs over the past few years have helped the bank steadily reduce gross NPAs from 9.25% in March 2004. Provision coverage stands at 72.9% excluding technical write-offs. This is above RBI's prescribed guideline of 70%. Slippage ratio further declined in 1QFY11 to an annualized rate of 0.62%, which, we expect, would go up in coming quarters as some loans from restructured assets portfolio may slip into the NPA category. Hence, we anticipate further stress on the bank's profitability, which we have modeled in our financial projections.

Fig. 10: Asset quality in comfortable zone



Source: Company, AMSEC

- **Steady improvement in restructured assets portfolio**

The bank has Rs32.4bn of assets under restructured categories, which constitute ~4.3% of its advances, below the industry average.

Allahabad Bank is demonstrating steady improvement in its restructured assets portfolio as it recovered Rs8.3bn from this segment until June 2010. Under RBI's special guidelines, the bank has restructured loans of ~Rs42.5bn, which constitute ~6.9% of its advances as of Jun 09.

Fig. 6: Restructured assets details

(Rs mn)	Mar 2010	Jun 2010	As % of Restructured Assets	As % of Total Advances	Slippage to NPA
Real Estate	6,780	6,160	19.00	0.81	350
Iron & Steel	3,380	3,710	11.44	0.49	110
Infrastructure	4,150	3,630	11.20	0.48	-
Agriculture	2,770	2,560	7.90	0.34	110
Engineering	2,310	2,290	7.06	0.30	30
Textiles	1,910	1,880	5.80	0.25	60
Housing	2,020	1,850	5.71	0.24	190
Sugar	1,880	1,530	4.72	0.20	-
Hotel	1,310	1,330	4.10	0.18	-

Fig. 7: Sector-wise restructured assets

	Jun-09	Mar-10	Jun-10
- Standard		32,170	30,730
- Sub-Standard		1,780	1,580
- Doubtful		250	120
Total Restructured Assets	**40,690**	**34,200**	**32,420**
- SME Debt Restructuring		2,930	3,330
Net Recovery from Restructured Assets		6,490	1,780
O/S Restructured assets as % of Total Advances	5.37	4.72	4.28

Source: Company, AMSEC

Around 4.8 % of restructured assets has already slipped into the NPA category and we expect some more assets to slip into this category in the coming quarters. We have conservatively modeled ~10% of the restructured loans as NPAs in our FY11 and FY12 estimates. We have placed gross and net NPAs at 1.49% and 0.58% by end-FY11 and estimate the bank to achieve provisioning cover (excluding technical write-offs) of 70-71% of gross NPAs in the coming years.

The bank has adequate head room to raise tier II capital (~Rs26bn) if required, to support more-than-expected credit growth

The bank is targeting 15% growth in core fee-based income in FY11.

- **Well capitalized to support growth**
  The bank is well capitalized and in a position to meet lending targets for the next two years. At end Q1FY11, CAR stood at 13.55% and tier I ratio was 8.24%, well above the required regulatory limit.

- **Healthy growth in fee and other income**
  We expect improvement in the bank's core fee businesses such as commission, fee and brokerage as a result of continued focus on improving fee-based income. Subdued treasury gains may offset growth in other income, leading to marginal growth in overall other income.

- **Bottom line is expected to grow ~27% over FY10-12**
  We expect Allahabad Bank's net profit to grow at a healthy 27% CAGR over FY10-12. However, net profit may see some pressure due to expected increase in loan loss provisioning expenses.

Fig. 11: Profit to grow at a healthy pace

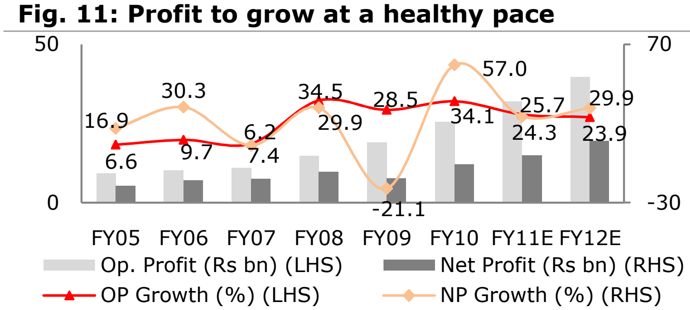
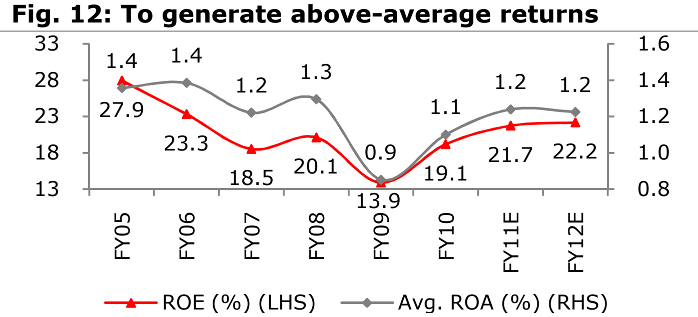


Fig. 12: To generate above-average returns



Source: Company, AMSEC

The bank's ROE and ROA will improve gradually in FY11; ROA would improve to 1.25% and ROE would increase ~300 basis points in FY12E as a result of strong growth in business and core operating performance.

Peer Comparison

	Allahabad Bank*	Andhra Bank	Central Bank	Corp. Bank	IOB	Indian Bank*	Oriental Bank*	Synd Bank	UCO Bank*	United Bank *	Vijaya Bank
Business Profile											
Deposit (Rs. bn)	1,083	747	1,546	910	1,095	910	1,231	1,086	1,189	667	627
YoY % Growth	21.2	22.6	13.1	26.2	8.6	18.6	19.8	(6.7)	18.4	11.6	14.2
Credit (Rs. bn)	757	571	1,076	648	830	680	861	941	817	446	419
YoY % Growth	24.1	27.2	23.1	36.8	7.9	30.9	20.3	12.8	19.5	12.7	13.7
CASA (%)	34.4	29.6	34.2	24.1	33.0	33.3	25.8	31.2	25.8	24.0	24.1
CD Ratio (%)	69.9	76.5	69.6	71.2	75.8	74.8	70.0	86.6	68.8	66.9	66.9
CRAR (%)	13.6	13.3	12.8	15.1	14.2	12.5	12.4	12.4	13.6	13.0	14.7
Tier I (%)	8.2	7.8	6.6	8.6	8.3	10.3	9.3	8.3	7.5	8.6	10.1
Profitability Matrix (FY10)											
NII (Rs mn)	26,505	21,947	25,453	22,103	31,679	33,039	29,074	27,398	23,241	13,912	14,491
YoY % Growth	22.8	34.9	14.2	30.7	10.4	26.7	45.6	7.5	41.3	19.8	28.8
Other Income (Rs mn)	15,159	9,646	17,352	11,864	11,433	11,737	12,001	11,675	9,659	5,587	6,795
YoY % Growth	32.8	26.0	62.2	7.2	(28.4)	13.4	12.0	27.6	(5.3)	13.8	(2.8)
Oper. Profit YoY % Growth	34.1	40.5	43.3	22.0	(30.2)	33.6	45.0	12.1	41.9	29.3	17.6
Net Profit (Rs mn)	12,063	10,459	10,582	11,703	7,070	15,550	11,347	8,133	10,122	3,224	5,073
YoY % Growth	57.0	60.1	85.3	31.1	(46.7)	24.9	27.4	(10.9)	81.5	74.5	93.3
Profitability Matrix - 1QFY10											
NII (Rs mn)	8,503	7,363	11,185	6,976	9,063	9,267	10,572	9,638	9,370	5,086	4,449
YoY % Growth	35.2	66.8	93.8	49.2	17.9	25.6	118.4	70.6	119.4	93.2	47.9
Other Income (Rs mn)	3,695	2,381	3,936	3,593	2,307	3,502	3,919	4,369	2,522	1,415	2,029
YoY % Growth	23.8	14.4	59.2	35.0	7.4	(1.5)	82.5	102.9	32.8	17.3	18.9
Oper. Profit YoY % Growth	19.3	46.7	84.9	19.7	(10.9)	32.9	59.1	13.8	108.1	109.8	49.8
Net Profit (Rs mn)	3,471	3,204	3,368	3,338	2,004	3,682	3,633	2,654	2,602	1,079	1,735
YoY % Growth	14.6	25.1	26.2	27.8	(33.6)	11.0	41.1	1.5	45.5	53.5	21.0
Key Profitability Ratio - 1QFY10											
NIM (%)	3.10	3.72	2.86	2.62	2.90	3.71	3.34	3.09	3.07	2.98	2.90
Non Int Inc as % of Op Income	25.99	22.04	18.10	27.61	19.16	27.72	16.88	18.26	16.85	19.17	27.73
Cost to Income Ratio (%)	38.67	45.96	51.12	35.62	65.95	34.65	35.35	50.20	42.71	45.85	48.95
Pro Burden as % of Op Profit	21.44	10.19	29.33	20.41	20.13	41.05	27.72	39.96	57.92	49.85	19.34
Assets Quality - 1QFY10											
Gross NPA (Rs mn)	11,393	5,793	26,111	7,268	35,709	9,884	14,951	21,748	19,291	14,216	9,728
Net NPA (Rs mn)	3,084	1,698	8,154	2,758	17,944	5,114	6,159	9,850	9,191	7,931	5,609
Gross NPA Ratio (%)	1.50	1.01	2.43	1.11	4.30	1.45	1.74	2.31	2.36	3.19	2.32
Net NPA Ratio (%)	0.41	0.30	0.77	0.43	2.21	0.76	0.72	1.06	1.14	1.80	1.35
NPA Coverage (%)	72.93	70.69	68.77	62.06	49.75	48.26	58.81	54.71	52.36	44.21	42.34
Efficiencies Level											
Number of Branches	2,316	1,560	3,606	1,159	2,002	1,762	1,526	1,508	2,156	1,558	1,534
Business per Branch (Rs mn)	795	845	727	1,345	961	903	1,371	1,344	931	714	682
Profit per Branch (Rs mn) Mar 2010	5.2	6.7	2.9	10.1	3.5	8.8	7.4	5.4	4.7	2.1	3.3
Per Share Data & Valuation											
CMP (Rs)	234	167	202	690	138	282	467	121	117	122	84
M.Cap (Rs bn)	104.5	81.0	81.5	99.0	74.9	121.1	116.9	63.3	64.4	38.6	36.3
Adjusted BVPS (1Q FY11))	121.2	89.0	90.0	388.8	79.9	151.3	263.3	81.6	48.2	67.1	40.1
BVPS (Rs) FY10	151.2	90.9	108.0	402.6	116.5	183.2	328.8	100.1	73.9	106.0	53.5
FY11E	178.3	112.6	144.8	453.7	120.9	215.4	382.0	102.6	92.4	118.5	70.0
FY12E	214.9	135.5	177.9	527.6	139.0	255.7	456.6	113.7	119.5	136.8	83.2
EPS (Rs) FY10	27.0	21.6	24.7	81.6	13.0	36.2	45.3	15.6	18.4	10.2	11.7
FY11E	33.6	24.6	33.9	88.1	15.0	40.4	61.3	18.9	23.9	15.4	12.9
FY12E	43.6	29.7	43.1	108.5	22.1	48.6	83.4	23.0	33.3	21.8	14.4
RoE (%) FY10	19.1	26.0	25.6	21.9	11.5	21.3	14.5	16.6	24.9	10.4	19.0
FY11E	21.7	23.9	21.5	20.1	12.2	20.3	17.3	17.2	25.9	14.8	17.6
FY12E	22.2	23.9	23.1	21.1	15.9	20.6	19.9	18.0	27.9	17.1	16.8
RoA (%) FY10	1.10	1.39	0.66	1.24	0.53	1.68	0.91	0.62	0.81	0.46	0.76
FY11E	1.2	1.2	0.9	1.0	0.6	1.6	1.0	0.7	1.0	0.7	0.7
FY12E	1.2	1.2	0.8	1.0	0.8	1.6	1.1	0.7	1.0	0.7	0.7
P/ABV (%) 1QFY10 (MRQ)	1.93	1.88	2.24	1.77	1.72	1.86	1.77	1.49	2.43	1.82	2.09
P/BV (%) FY10	1.55	1.84	1.87	1.71	1.18	1.54	1.42	1.21	1.59	1.15	1.57
FY11	1.31	1.48	1.39	1.52	1.14	1.31	1.22	1.18	1.27	1.03	1.20
FY12	1.09	1.23	1.13	1.31	0.99	1.10	1.02	1.07	0.98	0.89	1.01

Source: Companies, RBI, Bloomberg, AMSL Research;

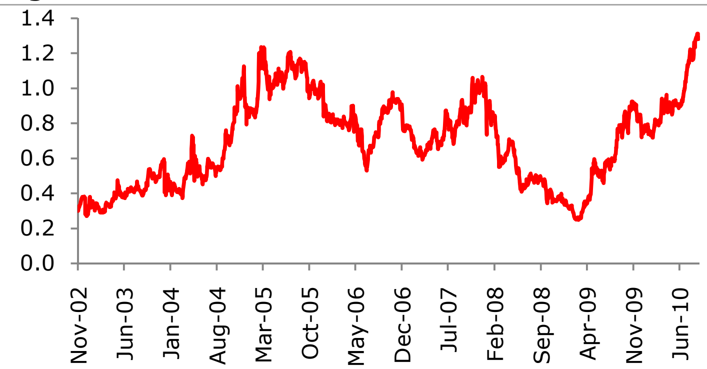
Note Estimates for Allahabad Bk, Indian Bk, OBC, UCO Bk and United Bk are AMSEC estimates and remaining all are Bloomberg consensus estimates*

Valuation

- **Valuation upgrade imminent ; Initiate with BUY**
  Allahabad Bank is on a strong growth trajectory and it is expected to outperform the Indian banking industry. It is expected to deliver healthy results in coming quarters, underpinned by strong growth in core operating income. We estimate earnings to grow at 27% CAGR over FY10-12, led by improvement in NII and healthy fee income growth. We have adopted a conservative stance on asset quality and we have factored in higher credit costs in FY11.

Fig. 13: 1 Year Forward P/E

Fig. 14: 1 Year Forward P/B



Source: : Company, AMSEC

The valuation charts show that Allahabad Bank has traded above 1x P/BV over the past few years. We expect a re-rating, supported by improved financial performance. In our view, Allahabad Bank's valuations will improve, as it is expected to generate sustained and improved return ratios among peers. We believe the market has not fully recognized the bank's fundamental strengths and it deserves a re-rating. We expect ROE of ~22% over the next two years and assign P/ BVPS of **1.5x to FY12E** book value.

We arrive at a target price of Rs293, which implies 25% potential upside from the current market price. We believe the stock is attractively valued at 1.31x of FY11E book value of Rs159 and 1.09x of FY12E book value of Rs195.5. We recommend **'BUY'** with a one-year target price of **Rs293.**

Risks to target price

- **Asset quality may deteriorate**
  The bank restructured substantial corporate and SME loans under RBI's special dispensation. These loans may slip into NPA categories, elevating the bank's credit risk.
- **Sharp decline in credit growth may hamper earnings growth**
  Credit disbursement by the banking system has recovered remarkably in the current fiscal year after dipping to 17.6%. If credit growth does not pick up to 20-22% over FY11, along with the overall banking industry, Allahabad Bank's profitability may suffer.
- **Rise in benchmark bond yield may affect profitability**
  Allahabad Bank's bond portfolio is immune to MTM losses approximately up to 8.1% of benchmark G-sec yields. Any movement of G-Sec yield above these levels may negatively impact the bank's profitability.

Financial Analysis

- **Healthy performance led by NII growth**
  Allahabad Bank demonstrated healthy financial and operating performance during 1QFY11. Net profit grew 14.6% YoY and 54.6% QoQ to Rs3.5bn, led by strong growth in NII and core fee income, partially offset by surge in loan loss provision expenses. Core operating income (ex treasury profit) grew 63.9% Rs6.2bn.

- **Strong growth in core fee income**
  During 1Q FY11, the bank reported strong growth of 16.23% YoY in core fee income to Rs1.7bn, compared with Rs1.47bn in the year-ago period. This growth was primarily due to 74.3% growth in LC/BG commissions, which was partially offset by decline in other fee income.

  On an aggregate basis, other income declined 19.2% YoY in 1QFY11 to Rs900mn due to a sharp 58% decline in treasury profit to Rs2.2bn. Non-interest income contributed 26% to total operating income in 1QFY11, compared with 37% in 1QFY10.

- **Operating profit up 19.3% YoY in 1Q FY11**
  Improvement in cost to income ratio resulted in strong growth in operating profit in 1QFY11. Cost to income ratio improved to 38.7% in 1QFY11 compared with 40.9% in 1QFY10. Operating expenses grew 8.9% to Rs4.4bn in the quarter.

Table 8: Financial Summary

(Rs.mn)	1QFY11	1QFY10	4QFY10	YoY %	QoQ %	FY10	FY09	YoY %
Interest Income	24,031	20,082	22,066	19.7	8.9	83,692	73,647	13.6
Interest Expended	15,528	13,791	14,640	12.6	6.1	57,187	52,061	9.8
Net Interest Income	8,503	6,291	7,426	35.2	14.5	26,505	21,587	22.8
Other Income	2,986	3,695	4,020	(19.2)	(25.7)	15,159	11,419	32.8
Operating Income	11,489	9,986	11,446	15.1	0.4	41,664	33,006	26.2
Operating Expenses	4,443	4,079	4,867	8.9	(8.7)	16,178	13,994	15.6
Operating Profit	7,046	5,906	6,580	19.3	7.1	25,486	19,012	34.1
Provisions and Contingencies	1,511	396	2,972	281.2	(49.2)	7,769	8,254	(5.9)
Pre tax Profit	5,535	5,510	3,608	0.5	53.4	17,716	10,758	64.7
Provisions for Tax	2,064	2,481	1,363	(16.8)	51.4	5,542	2,970	86.6
Net Profit	3,471	3,029	2,245	14.6	54.6	12,063	7,686	57.0

Source: Company, BSE,

- **Strong traction in business**
  Allahabad Bank reported strong growth in business in 1QFY11: 24.12% YoY growth and 4.53% QoQ growth in credit to Rs757.2bn and 21.2% YoY growth and 2.13% QoQ growth in deposits to Rs1,083bn.

- **Asset quality remains stable**
  Allahabad Bank has been able to maintain comfortable asset quality. Gross NPA and net NPA ratios in 1QFY11 were 1.45% and 0.76% compared with 0.91% and 0.40% respectively. Provision coverage was 73% excluding technical write-offs, which is way above the RBI's prescribed guidelines of 70%.

Table 9: Key Quarterly Numbers

Quarter Ended	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
Deposit (Rs. bn)	751	850	894	873	942	1,061	1,083
Advance (Rs. bn)	528	594	610	608	657	724	757
CD Ratio (%)	70.2	70.0	68.2	69.6	69.8	68.3	69.9
Incremental CD Ratio (%)	71.7	67.7	35.2	9.9	71.3	56.8	144.9
Assets Quality							
Gross NPA (Rs. mn)	10,160	10,782	10,931	10,821	11,605	12,218	11,393
Net NPA (Rs. mn)	4,292	4,191	2,198	2,084	2,275	4,702	3,084
% of Gross NPAs	0.92	0.89	0.91	0.89	0.89	0.81	1.45
% of Net NPAs	0.16	0.18	0.40	0.18	0.16	0.23	0.76
Profitability							
NIM (%)	3.2	3.0	3.0	2.8	3.0	3.0	3.1
Other Income as % of OI	40.3	43.6	37.0	40.2	33.4	35.1	26.0
Cost to Income Ratio (%)	34.2	41.6	40.9	35.5	36.0	42.5	38.7
Pro Burden as % of Op Profit	15.5	41.3	6.7	29.8	37.9	45.2	21.4

Source: Company

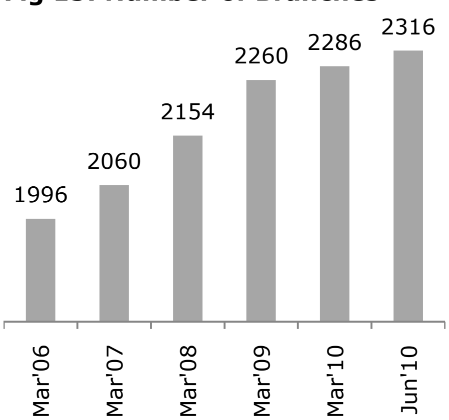
Business profile

Allahabad Bank Ltd is a Kolkata-headquartered Public Sector Bank (PSB) with an asset size of ~Rs1,217bn and network of 2,316 branches. The bank has a pan-Indian presence with a strong foothold in eastern and northern India. It was incorporated in 1865 by a group of Europeans and it is the oldest existing joint stock bank in India. In 1923, the bank shifted its headquarters to Kolkata in 1923. Allahabad Bank was nationalized in 1969 by GoI along with 13 other major commercial banks. The bank made an initial public offering (IPO) in 2002 and a follow-on public issue in 2005.

Allahabad Bank's total business touched Rs1,840bn as of June 30, 2010, with deposits in excess of Rs1,083bn and advances of Rs757bn. Its credit-deposit ratio stood at 69.9% in 1Q FY11. The bank's deposits and advances grew at 27.6% and 21.8% CAGR respectively during FY2005-10. Its capital adequacy ratio stands at 13.5% at end 1QFY11 with healthy Tier-1 capital ratio of 8.24%.

Allahabad Bank has a strong and experienced team headed by **Mr. J P Dua**, which has steered it well during challenging times. Mr. Dua was promoted from Executive Director to CMD of the bank after the Government transferd Mr. KR Kamat to Punjab National Bank. A strong and stable management team reinforces confidence in the bank's ability to deliver balanced growth.

Fig 15: Number of Branches



Source: Company

Subsidiaries

AllBank Finance: AllBank Finance Ltd (ABFL) is Allahabad Bank's wholly-owned subsidiary; it is involved in investment banking and other corporate fee-based activities. AllBank Finance Ltd reported revenue of Rs106.93bn and profit of Rs71.4bn in FY10.

Associates

Universal Sompo General Insurance: Universal Sompo is a joint venture between Allahabad Bank, Indian Overseas Bank, Karnataka Bank Limited, Dabur Investments and Sompo Japan Insurance Inc. with share of 30%, 19%, 15%, 10% and 26% respectively.

Allahabad Bank – Financial Summary

Profit & Loss Statement

Rs Mn	FY09	FY10	FY11E	FY12E
Interest Earned	73,647	83,692	101,772	124,889
Interest Expenditure	52,061	57,187	67,573	82,866
Net Interest Income	21,587	26,505	34,199	42,023
Other Income	11,419	15,159	16,504	19,146
Net Operating Income	33,006	41,664	50,702	61,169
Operating Expenses	13,995	16,178	18,675	21,496
Operating Profit	19,012	25,486	32,028	39,673
Provisions & Contingencies	8,254	7,769	10,600	11,843
Tax Expenses	3,072	5,653	6,428	8,349
Adjusted Net Profit	7,685	12,067	14,999	19,481

Balance Sheet

Rs Mn	FY09	FY10	FY11E	FY12E
Capital And Liabilities				
Capital	4,467	4,467	4,467	4,467
Reserves Total	54,053	63,063	75,187	91,532
Deposits	849,718	1,060,558	1,256,761	1,508,113
Borrowings	38,489	54,355	68,202	85,473
Other Liabilities & Provisions	29,753	34,550	40,769	48,108
Total Liabilities	976,480	1,216,992	1,445,386	1,737,692
Assets				
Cash & Cash Equivalents	66,368	91,682	99,451	118,118
Investments	296,511	384,286	429,812	514,266
Advances	588,018	716,049	887,900	1,074,359
Fixed Assets	11,098	11,183	12,301	13,531
Other Assets	14,487	13,792	15,922	17,417
Total Assets	976,480	1,216,992	1,445,386	1,737,692

Per Share Data and Valuation

	FY09	FY10	FY11E	FY12E
No. of Shares (mn)	447	447	447	447
Earnings Per Share (Rs.)	17	27	34	44
Book Value Per Share (Rs.)	131	151	178	215
Adj. Book Value/Share (Rs.)	102	121	147	182
Dividend Per Share (Rs.)	2.50	5.50	5.50	6.00
Price/ Earnings (X)	2.26	5.29	6.97	5.37
Price/ BV (X)	1.79	1.55	1.31	1.09
Price/Adjusted BV (X)	0.38	1.18	1.59	1.28

Adequacy Ratio (%)

	FY09	FY10	FY11E	FY12E
Total CAR	13.14	13.63	13.88	13.86
Tier 1	8.04	8.12	8.23	8.12

Ratio

	FY09	FY10	FY11E	FY12E
Growth Ratio YoY (%)				
Advances	18.3	21.8	24.0	21.0
Deposits	18.6	24.8	18.5	20.0
Net interest Income	29.1	22.8	29.0	22.9
Fee Income	18.4	32.7	8.9	16.0
Provisions Expense	131.0	-5.9	36.4	11.7
Net Profit	(21.2)	57.0	24.3	29.9
ROA Decomposition (%)				
NII / Assets	2.2	2.2	2.4	2.4
Other income / Assets	1.2	1.2	1.1	1.1
Net Income / Assets	3.4	3.4	3.5	3.5
Operating Profit / Assets	1.9	2.1	2.2	2.3
Return on Avg Assets	0.9	1.1	1.2	1.2
ROE	13.9	19.1	21.7	22.2
Yields / Margins (%)				
Average Yield on funds	9.0	8.3	8.3	8.4
Average cost of Funds	6.3	5.7	5.5	5.7
Interest Spread	2.6	2.6	2.7	2.8
Net Interest Margin	2.4	2.4	2.6	2.6
Earnings Quality (%)				
Net Int. Inc/Net Income	65.4	63.6	67.5	68.7
Fee Income /Opr. Profit	60.1	59.5	51.5	48.3
Cost/Income	42.4	38.8	36.8	35.1
Effective Tax Rate	13.1	28.6	30.0	30.0
Balance Sheet Ratio				
Credit / Deposit Ratio	69.2	67.5	70.6	71.2
Incremental C/D Ratio	68.0	60.7	73.7	74.2
Investment-Deposit Ratio	34.9	36.2	34.2	34.1
Investment / Assets	30.4	31.6	29.7	29.6
Cash-deposit Ratio	6.0	6.8	6.1	6.0
CASA Ratio	34.6	34.5	35.5	36.5
Gearing (Assets / Equity)	16.7	18.0	18.1	18.1
Asset Quality (%)				
Gross NPA/ Gross Advances	1.83	1.71	1.49	1.45
Net NPA/Net Advances	0.72	0.66	0.58	0.55
Provisioning Burden as % of PPP	43.41	30.49	33.10	29.85
Loan Loss Reserves / Gross NPA	59.51	61.52	119.57	172.31
Loan Loss Reserves / Total Loans	1.09	1.05	1.78	2.50

Raising the bar

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